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USDOC FOR 4430/MAC/EAP/M.HOGGE
TREASURY FOR OASIA AND IRS
GENEVA FOR USTR

E.O. 12958: N/A
TAGS: EFIN EINV ECON ETRD PREL MY BG
SUBJECT: MALAYSIAN PM ANNOUNCES FINANCIAL SECTOR
LIBERALIZATIONS

REF: KUALA LUMPUR 303

¶1. (U) Summary: Prime Minister Najib Tun Razak announced a number of liberalizations to Malaysia's financial sector on April 27, as promised last week when he removed some restrictions in various service sectors (reftel). Foreign equity limits will be raised from 49 percent to 70 percent for investment banks, Islamic banks, and insurance companies, but will remain capped at 30 percent for domestic commercial banks. Up to seven new licenses will be given to foreign banks over the next three years, including two Islamic banks, two commercial banks with "specialized expertise," and three "world-class" commercial banks that can offer "significant value propositions to Malaysia." Up to two new licenses will be issued for Islamic insurance providers. Some "operational flexibilities" will be offered to foreign and domestic financial service providers and offshore companies. Central Bank Governor Dr. Zeti Akhtar Aziz told the press that these measures bring Malaysia in line with 90 percent of reaching the goals laid out in the ten-year Financial Sector Master Plan, established in 2001. The full liberalization package can be found at www.bnm.gov.my.

¶2. (SBU) Comment: Reactions among financial sector professionals and economic analysts ranged from tepid praise to expressions of real hope for the Malaysian economy going forward. Najib seems to be carefully selecting reforms that will be less painful for his closest supporters and for the average voter. Nevertheless, as with the liberalizations to the services sector he announced last week, Najib is sending a message to the business community and the public that he is determined to move on necessary reforms and that may be even more important than the near-term economic impact of the announced measures. End comment.

ISSUANCE OF NEW LICENSES

¶3. (SBU) In line with the GOM's goal of making Malaysia a global hub for Islamic finance, the government will offer up to two new licenses for foreign Islamic banks with a minimum paid-up capital of USD 1 billion. In addition, two new licenses will be granted for "family takaful" (Islamic life and investment insurance). AIG Chief Executive Officer for Southeast Asia Rob Ryan told Econoff that his company was

definitely interested in obtaining a license to offer Islamic insurance products in Malaysia and had been in discussions with the central bank for some time.

¶4. (SBU) Two new commercial bank licenses will be offered by the end of 2009 to foreign banks with "specialized expertise." Sanjeev Nanavati, CEO of Citibank Malaysia, told EconCouns that he believed the GOM was looking for banks with expertise in financing infrastructure projects, shipping, and agriculture. He named Robobank and Fortis as two possibilities.

¶5. (SBU) Another three commercial banking licenses would be offered in 2011 to "world-class banks that can offer significant value propositions to Malaysia." The GOM provided no details, but Dr. Yeah Kim Long, Managing Director and Chief Economist for Rating Agency Malaysia speculated that, while the Islamic banking licenses were intended to draw money from the Middle East, Malaysia also was looking to India and China as it saw those markets as areas of growth.

FOREIGN EQUITY LIMITS

¶6. (SBU) Foreign equity limits were raised from 49 percent to 70 percent for investment banks, Islamic banks, and insurance companies. Yeah pointed out that since few American financial service companies were in any position to make acquisitions, this was a relatively safe time to raise equity limits. Even Middle Eastern banks were having liquidity problems. Still, if Malaysia wanted to become a global hub for Islamic finance, liberalization was a necessity. He said domestic Islamic banks already were facing stiff competition

from the new foreign Islamic banks licensed in the last several years, and taking foreign partners not only would force them to improve their own competitiveness, but also would give them inroads into other countries.

PERMISSION TO OPEN NEW BRANCHES

¶7. (SBU) Citi's Nanavati was most optimistic about a new provision to allow locally-incorporated foreign banks (like Citi) to establish four additional branches: one in an urban area, two in semi-urban areas, and one in an underserved rural area. Negotiating the locations of these branches was "manageable," he told EconCouns. He did not expect Citi to take advantage of a new provision to allow the establishment of up to ten "microfinance branches" in the near term. Suhaimi Ilias, Vice President and Chief Economist for Equity Markets at Maybank Investment Bank highlighted microfinance as one of the areas of "specialized expertise" the GOM wanted to attract to Malaysia. The day before Najib's announcement, Suhaimi speculated that perhaps Bangladesh's Grameen Bank would be opening up shop in Malaysia. Ryan said a provision to lift branching restrictions on insurance companies altogether was a welcome relief; AIG has been in negotiations with the central bank for some time just to get permission to move several of its branches. Ryan also welcomes the lifting of restrictions in employing expatriates; currently AIG is limited to three expatriate work visas in addition to the CEO. Nanavati explained that the central bank already had lifted the numerical restrictions on the banking sector regarding how many expatriates it could hire.

OFFSHORE COMPANIES TO OPEN OFFICES IN KUALA LUMPUR

¶8. (U) Holding companies in Labuan, Malaysia's offshore financial services center, will be allowed to establish offices in Kuala Lumpur, subject to approval from the Labuan Offshore Financial Services Authority (LOFSA). The Kuala Lumpur office will be allowed to trade outside Malaysia as well as hold investments, provide management services, manage surplus funds, and provide credit facilities to related companies within Malaysia or non-related companies outside Malaysia, subject to some restrictions. Details are

available at www.lofsa.gov.my.

OVERALL REACTION: POSITIVE, BUT NOT WITHOUT DISAPPOINTMENTS

¶9. (SBU) Overall, reactions to the announced liberalizations were positive. Yeah was optimistic that the PM would continue liberalizations at a "sustained pace" up until the next election in 2013, explaining that even many young Malays were seeing that affirmative action programs, while effective in the short run perhaps, were counterproductive in the long run. Yeah told Econoff that the 2004 landslide victory for the current ruling coalition was based on promises of then-Prime Minister Abdullah to clean up corruption and reform the economy. He attributed the drop in support and the loss of five states in the March 2008 elections to the fact that those promises never materialized. "Now the ruling party and the opposition are competing on the basis of who can be the biggest reformer, and if Najib doesn't reform, he'll lose the next election," he said.

¶10. (SBU) Yeah told Econoff that PM Najib seemed to have hand-picked the liberalization measures that would be the least painful) both in terms of exposing domestic players to competition and with regard to the man on the street. Yeah described the measures as "carefully paced to meet the public,s expectations." While the impact of the reforms on the overall economy was likely to be small, they made a significant impact on "sentiments" because they represented a breach of the race-based policies and the system of protecting domestic players.

¶11. (SBU) There were some disappointments as well. Ryan told Econoff that AIG and other insurance providers in Malaysia had been in discussions with the central bank for some time

to remove the ceiling on premiums for auto and fire insurance, neither of which had been raised since 1974. Auto and fire policies comprised 60 percent of general insurance premiums, he explained, and while fire insurance still generated a modest profit, auto insurance was a loss maker for most insurance companies in Malaysia. Discussions about lifting premium caps had been ongoing, he said, but no proposals were on the table. Ryan speculated that licenses for new banks and liberalizations for various technical matters in the banking sector had little political impact for the man on the street, but automobile insurance premiums were a different matter, and more likely to be remembered by voters.

KEITH